BRIEF IN SUPPORT OF PETITION.

OPINIONS OF THE COURTS BELOW.

The opinion of the District Court (R. 186-195) is reported in 28 Fed. Supp. 227.

The opinion of the Circuit Court of Appeals is reported in 113 Fed. (2d) 64.

ARGUMENT.

The petitioner claims to be entitled to the deduction—

> (1)—Under subparagraph a (4), on the ground that neither the estate nor she as beneficiary claimed the deduction in their returns filed for 1926, or in any other year (Petition, Par. 6th, admitted by answer, R. 15), and that she paid the California inheritance tax;
>
> or
>
> (2)—Under subparagraph a (5), on the ground that a claim for the deduction by the estate is barred by the statute of limitations, and she is entitled to the deduction whether she paid the tax or the estate paid it.

I.

PETITIONER PAID THE CALIFORNIA INHERITANCE TAX AND IS ENTITLED TO RECOVER UNDER SUBPARAGRAPH A (4) OF SECTION 703 OF THE REVENUE LAW OF 1928.

Paragraph Sixth of the petition, admitted by the answer (R. 15) avers that—

> "The said item of $92,451.56 was not claimed as a deduction against gross income in the income tax return which was filed by the Executors under the last will and testament of D. Herbert Hostetter, Deceased, for the calendar year 1926, or in the fidu-

ciary return which was filed for the calendar year 1926 by the Trustees under the last will and testament of D. Herbert Hostetter, Deceased, and was not claimed as a deduction by the petitioner in the income tax return filed by her for the year 1926, or in any other year or years."

This admission by the answer established conclusively that no deduction has been claimed by the estate or by the beneficiary in 1926, or in any other year.

The only other requirement under subparagraph (4) is that the petitioner be the person by whom the California tax was paid.

The opinion of the Circuit Court of Appeals holds that:

(1)—The California inheritance tax is imposed "upon the right to inherit rather than the right to transit".[1]

(2)—In the report of the California state inheritance tax appraiser, the order of the probate court approving the appraisal, and the tax receipt issued by the treasurer of Los Angeles County, "the tax is treated as being due by the beneficiaries."

(3)—The provisions in the California act that the executors shall deduct the tax before paying the shares to the beneficiaries, etc., are "obviously designed for the effective collection of the tax rather than to fix the liability for the tax upon the estate".

From these rulings, we submit, it follows that the California tax was owed by the beneficiaries, and not by the estate.

While so ruling, the opinion adds that it does not necessarily follow from the fact that the petitioner as

---

1. So held in *United States v. Kombst,* 286 U. S. 424; *Estate of Miller,* 184 Cal. 674; *Estate of Watkinson,* 191 Cal. 591; *Estate of Rath,* 10 Cal. (2d) 399.

beneficiary was ultimately liable for the California inheritance tax, that the petitioner in fact paid the tax in 1926.

We submit, however, that the presumption would be that the payment was made by the party ultimately liable.

The ruling of the Circuit Court of Appeals, we submit, is contrary to many decisions in which a state inheritance tax was imposed upon the beneficiary but was paid by the executor out of the estate and later the executor either deducted the amount of the tax from the share of the beneficiary or was reimbursed by the beneficiary for the payment. In these cases, it has been held that the tax was in fact paid by the beneficiary and he was entitled to deduct the same in his income tax return.

Our case is even clearer, because, as we shall show in detail hereafter, the trustees of the estate made a loan to the beneficiary and with this money the beneficiary paid the tax.

In this case, the Circuit Court of Appeals said:

"The District Court found from the documentary evidence that the estate in fact paid the tax. We do not believe this finding was erroneous." *As we read the agreement* of January 15, 1926, it provided that the tax be paid with funds advanced for that purpose by the Pennsylvania executors and trustees of the estate. It is true that the executors safeguarded the estate from loss and themselves from surcharge by requiring that the life tenants release their respective interests in income equal to the taxes and execute non-negotiable promissory notes payable in installments over a period of ten years. The emphasis throughout the agreement,

however, is that the executors should pay the tax. We think it may fairly *be concluded* that the petitioner did not borrow the money and then use the borrowed funds to pay the taxes, but that the executors paid the taxes and the petitioner promised to reimburse them."

It clearly appears, therefore, that—

(a)—The conclusion of the Appellate Court was based upon the interpretation of the agreement under which moneys were "advanced" by the Trustees, and—

(b)—The finding is merely a conclusion from documentary evidence and is a legal interpretation of a written instrument, presenting a mixed question of law and fact.

A FINDING WHICH IS NOT BASED UPON DISPUTED TESTIMONY BUT IS AN INFERENCE OR CONCLUSION FROM WRITTEN RECORDS OR UNDISPUTED FACTS MAY BE REVIEWED BY AN APPELLATE COURT.

Greenfield v. Blumenthal, 69 Fed. (2d) 294, 298 (Certiorari denied in 292 U. S. 633);

In re Heilbron Bros., Inc., 226 Fed. 803, 804 (Affirmed by Circuit Court of Appeals in 229 Fed. 554);

Budd v. Commissioner of Internal Revenue, 43 Fed. (2d) 509, 512;

Washburn v. Commissioner of Internal Revenue, 51 Fed. (2d) 949, 951;

Bianchi v. Vere, 17 Fed. (2d) 22 (Certiorari denied in 274 U. S. 752);

Quinn v. Union National Bank, 32 Fed. (2d) 762.

Again, the opinion of the Circuit Court of Appeals says:

> "Without more, the fact that the entire tax assessed upon the value of the property in California was paid by one check, drawn by the Fidelity Title and Trust Company, an executor and trustee under the will, upon funds belonging to the corpus of the estate would justify the District Court's *conclusion* that the estate and not the beneficiaries paid the tax."

This statement, we submit, amounts to saying that the District Court might pick out this check, which was one of a number of documents comprising the entire transaction and entirely ignore the other documents which provided for the issuing of the check and declared the purpose for which it was issued. The requirement of substantial evidence to support a finding is not met by isolating one paper from other papers which show what was to be paid by the check and who was to pay.

As already stated, the presumption is that the payment was made by the party ultimately liable.

What evidence was there to rebut such presumption? The opinion relies upon (a) the check by which the tax was paid; and (b) the agreement of January 15, 1926.

The Check: The check was signed by the Fidelity Title and Trust Company merely, without any designation as executor or otherwise. This fact shows that the trust company was merely transmitting the money and was not acting in a fiduciary capacity.

The reverse side of the check bears the words "Fidelity Title and Trust Company, co-executor". This notation earmarks the deposit account against which the check is authorized to be charged.

The reverse side of the check further states that the check is:

> "in full for inheritance taxes—estate D. H. Hostetter, Decd. as shown per first and final account filed by Miriam G. Hostetter and Helene Hostetter, executrices" (R. 118).

This first and final account was offered in evidence as Exhibit 10, and stated that the executors had received

> "Advancements by beneficiaries under Last Will and Testament of D. Herbert Hostetter, deceased, to pay California State Inheritance Taxes 294,752.61" (R. 126).

This reference in the check to the account shows that the money came from the beneficiaries who borrowed it from the Pennsylvania trustees.

Our case, we submit, is stronger than several other classes of cases in which the inheritance tax was paid by the check of a fiduciary and out of the funds of the estate, and yet the tax was held to have been paid by the beneficiaries. In one class of cases, the amount of payment was deducted from the share of the beneficiary in the estate. In fact, this is done uniformly under a state statute which requires the executor to act as a collection agent and to see that the tax is paid to the state. In another class of cases, the trustees have filed a fiduciary return showing the payment of inheritance tax as a credit against the share of the beneficiary.

In each of these classes of decisions, the fiduciary pays the inheritance tax with his check as executor of

the estate and the check is paid out of the funds of the estate, and yet with no other explanation, the payment is held to be made by the beneficiary. The fact that the state law imposes a tax upon the beneficiary helps to support the conclusion.

Our case is stronger because the check is connected with and explained by other written instruments:

(a)—Before the check was sent, correspondence passed between the Pittsburgh attorneys and the California attorneys of this estate, and the California attorneys advised that the inheritance tax of that state was assessed against the beneficiaries under the will, but that it might be paid in the first instance by the executors, but must then be charged against the beneficiaries in the final account (Exs. 4 and 5, R. 111). This was the procedure in the classes of decisions just mentioned. The Pittsburgh attorneys then submitted in a letter (Ex. 8, R. 119), the procedure exactly as later carried out; the Pennsylvania trustees to loan the money to the beneficiaries and the beneficiaries to give their notes to the trustees for their respective shares of the tax. This loan was made necessary by the fact that the beneficiaries did not have the money (R. 66). The California attorneys advised their approval and that "the disbursements will actually be made in the last analysis by the beneficiaries themselves * * *" (Ex. 9, R. 121).

(b)—The receipt in which, the opinion of the Circuit Court of Appeals says, "the tax is treated as being due by the beneficiaries" (Ex. 2, R. 95).

(c)—First and final account filed by the California executors charged the executors with "advancements *by beneficiaries* * * * to pay California inheritance taxes 294,752.61". (Ex. 10, R. 126). In contrast with this the account charged the

executors with *advancements by the Fidelity Title and Trust Company* to pay expenses of administration. This difference shows unmistakably that the payment of the California tax was made by the beneficiaries and not by the estate.

(d)—Supplemental account filed by the Pittsburgh trustees listed the notes given by the beneficiaries as assets of the estate (Ex. 11, R. 126).

This listing of the notes as assets shows that they were treated by the Pennsylvania trustees as investments—that loans had been made by the trustees to the beneficiaries; and that these notes were not merely in the nature of indemnity given by the beneficiaries to the Pennsylvania trustees.

The Agreement of January 15, 1926: It recited that the California inheritance tax was charged against the various legatees and provided that a sum equal to the amount of the tax should be advanced by the Pennsylvania executors to the Pennsylvania trustees, and the trustees should then advance that sum to the California executors to pay the tax and further that the beneficiaries should then give their notes to the trustees for their respective share of the tax.

The trust company refused to forward the check to California unless this agreement was signed by the beneficiaries (R. 43).

In all this we find nothing except that the tax was advanced and paid by the fiduciary out of the funds of the estate, just as in the classes of decisions above mentioned.

In our case we do have a further and very distinctive provision:

The agreement required each beneficiary to give his note to the fiduciary for his share of the tax and provided that the notes should be paid by periodical deductions from the share of each beneficiary in the income.

This agreement and the notes, we submit, show that the beneficiaries were paying the tax. Otherwise, why would they sign such notes and obligate themselves to pay these large sums of money? The opinion suggests that in taking these notes, the executors safeguarded the estate from loss and themselves from surcharge. However, if such was the purpose, the agreement would have provided that the beneficiaries pay only in case of such loss, and in the absence of loss, the beneficiary would never have paid anything. Here, however, the beneficiaries bound themselves to pay periodically, loss or no loss, and actually did pay the full amounts of the notes.

Finally, we submit, that neither the check nor the agreement should be considered as evidence in itself, but each is inseparably connected with the other documents just summarized and is explained by them. These documents form one transaction and from them as a whole, the conclusion must be drawn as to who paid the California tax. Such a conclusion, we submit, does fall within the rule that an inference drawn from documentary evidence or uncontroverted facts may be reviewed whether supported by substantial evidence or not.

THE ORPHANS' COURT OF ALLEGHENY COUNTY, PENNSYLVANIA, HAVING JURISDICTION OVER THE ESTATE OF D. HERBERT HOSTETTER, DECEASED, REVIEWED THE SAME DOCUMENTARY EVIDENCE AND HELD THAT THE CALIFORNIA INHERITANCE TAX HAD BEEN ASSESSED AGAINST THE BENEFICIARIES AND HAD BEEN PAID BY THE BENEFICIARIES WITH FUNDS WHICH WERE LOANED TO THEM BY THE ESTATE.

In 1931 the executors of Frederick G. Hostetter, a son, filed a petition in the Orphans' Court of Allegheny County for a review of its decree of distribution of the estate of D. Herbert Hostetter. This petition (Ex. 14, R. 135) averred that the California tax was assessed against the interest of the life beneficiaries (Pars. 8, 9); that Frederick had given his note to the trustees for his share of the tax and the note had been partly paid by moneys withheld from his share of the income (Pars. 20, 19, 24); and that the life beneficiaries were not legally liable for the inheritance tax and that the tax was payable out of corpus without reimbursement from beneficiaries (Par. 22).

The petition prayed for a decree cancelling the note of Frederick given for his share of the tax and directing the trustees to refund to his estate the amounts retained from his share of income and applied on the note (R. 148). The Orphans' Court held that the California tax had been assessed against the beneficiaries and paid by them with funds loaned to them by the estate and refused reimbursement (Opinion, Ex. 15, R. 150).

II.

THE PETITIONER IS ENTITLED TO THE DEDUCTION UNDER SUBPARAGRAPH A (5).

The ruling of the Circuit Court of Appeals in regard to the subparagraph a (5) is contained in the following quotation from the opinion:

> "Clause (5) gives no comfort to the petitioner for there is nothing in the record other than an allegation in her complaint, which is denied in the answer, that at the time the petitioner filed her claim for refund the statute of limitations had run so as to bar the estate's claim to a deduction for the taxes which it had paid."

The petitioner respectfully suggests that the averment that any claim of the estate to the deduction was barred by the statute of limitations, was a legal conclusion. However, Paragraph Sixth of the petition (R. 3), admitted by the government's answer (R. 7), averred (omitting unnecessary words):

> "The said item of $92,451.56 was not claimed as a deduction against gross income in the income tax return which was filed by the Executors * * *, for the calendar year 1926, or in the fiduciary return which was filed for the calendar year 1926 by the Trustees * * *, or in any other year or years." (R. 3).

The words "in any other year or years", inserted at the end of Paragraph Sixth, are preceded by a comma, so that these words qualify the entire preceding portion of the sentence, including the allegation that

> "the said item of $92,451.56 was not claimed as a deduction."

The allegation, therefore, is that the said item of $92,451.56 was not claimed as a deduction by the executors or trustees in any other year or years.

The averment that the item was not claimed as a deduction in the income tax return *for* the year 1926 is in contrast with the words at the end "*in* any other year or years". This comparison shows that Paragraph Sixth is intended to say that no claim for a deduction was made in any year or years,—at all or in any manner, and not merely in a return.

The affidavit to the petition was made by the petitioner on January 18, 1934, (R. 8), and is therefore an averment, admitted, that prior to that date the item was not claimed as a deduction by the estate.

The statute of limitations applicable to this case is Sec. 322 (b) (1), which has been embodied in identical language in the revenue laws of 1934, 1936, 1938 and 1940, as follows:

> "(1) Period of Limitation.—Unless a claim for credit or refund is filed by the taxpayer within three years from the time the return was filed by the taxpayer or within two years from the time the tax was paid, no credit or refund shall be allowed or made after the expiration of whichever of such periods expires the later * * *."

The government's tenth request and the lower court's tenth finding, which are identical, are as follows:

> "10. Although the executors and trustees filed income tax returns for 1926, neither they nor plaintiff claimed the benefit of a deduction with respect to said $294,752.61 inheritance tax payment, or any part thereof, in their said returns." (R. 190)

Petitioner's claim for refund was rejected by the Commissioner of Internal Revenue on January 22, 1932, and her suit was filed on January 20, 1934. (4th Finding, R. 187). The averment admitted of Paragraph Sixth is therefore that no claim for deduction was made by the estate prior to January 18, 1934.

The period of three years from the date of filing the returns of the executor and trustee had elapsed before either of these dates.

Therefore, "the claim of the deduction by the estate is barred by the statute of limitations" within the language of subparagraph a (5).

The petitioner, Miriam G. Hostetter, filed on March 12, 1930 (3rd Find., R. 187), a claim for refund, asserting her right to this deduction in her income tax for 1926. This claim was rejected by the Commissioner on January 22, 1932, and this suit was instituted on January 20, 1934 (4th Find., R. 187). Therefore, the "claim by the beneficiary is not so barred" within subparagraph a (5).

Both conditions of subparagraph a (5) are therefore satisfied.

The last paragraph of the opinion, quoted above, objects specifically that the record does not show that, *"at the time the petitioner filed her claim for refund* the statute of limitations had run so as to bar the estate's claim to a deduction * * *." (Italics ours).

This interpretation of subparagraph (5), that the right of the beneficiary to the deduction must depend upon whether the right of the estate to the deduction is barred when the beneficiary's claim for refund is filed, we respectfully submit, is unsound, because—

(a)—***This interpretation would render subparagraph (5) virtually inapplicable, or useless.*** The returns of both the beneficiary and of the executor and trustee must be filed before the same date, March 15th, and the taxes must be paid by either before that date or quarterly. The dates are the same in each case and the period therefore within which the beneficiary may claim the deduction and the period within which the executor or trustee may claim the deduction, coincide. By the time the period for the estate to claim the deduction has expired, the period for the beneficiary to claim the deduction has also ended and the right of the beneficiary to claim is also barred.

In like manner the estate could not file a claim for the deduction under subparagraph a (5) until after the right of the beneficiary to claim the deduction has expired and the right of the estate also would be barred.

(b)—The result would be that in virtually no case could the beneficiary claim the deduction under subparagraph (5) in spite of the fact that the report of the conference committee of both houses on subparagraph (5) specifically says that subparagraph (5) was added by Senate amendment No. 210 to the Revenue Law of 1928 because—

> "* * * in order to *make it certain that the deduction will be allowed either to the estate or to the beneficiary in any event,* the Senate amendment allows the deduction to the estate if the beneficiary is barred from filing a claim for refund by the statute of limitations, and vice versa * * *" (Italics ours).

This report is quoted in the Appendix, *infra.* p. 35.

(c)—The context of Section 703 (a) itself and the committee reports show that the intention of

Congress was to enact remedial legislation of the most liberal character. This has been expressed in general counsel's memorandum 9490 (Cumulative Bulletin X-1, 208, 210), as follows:

"It is evident, both from the context of section 703, itself, and from the committee reports, that the intention of Congress was to enact remedial legislation of the most liberal character—legislation which would tend to do away with administrative difficulties in determining the precise character of the taxes in question, and which would eliminate litigation, or greatly reduce it, with respect thereto. In the language of the committee reports, the general plan for effecting this result was 'to make it certain that the deduction will be allowed either to the estate or to the beneficiary in any event' (subject to the statute of limitations), by prescribing rules which would tend 'to ratify what the taxpayers have done.' It is a familiar canon of statutory construction that remedial legislation of this character should be liberally construed."

The same opinion was expressed by the Board of Tax Appeals in *Marion S. B. Lansill,* 17 B. T. A. 413; and in *Frances E. B. Lentz,* 21 B. T. A. 1336, 1342.

(d)—The time when the claim of the estate to the deduction must be barred, we submit, is when the question of the right of the beneficiary to the deduction is to be *determined.* This determination will ordinarily be made, or could be deferred until, after the period of limitation has expired for both the beneficiary and the estate.

The grant of authority made in Sec. 703 to allow the deduction is contained in the initial words "In determining the net income of an heir * * * beneficiary * * * the amount of the estate * * * taxes * * * shall be allowed as the deduction

* * * if the claim of the deduction by the estate is barred by the statute of limitations, * * *."

The key words of Section 703 are "In determining". In our case, we submit, the determining occurred when the lower court made its decision.

Prior to the enactment of Sec. 703, the right to claim the deduction depended upon the interpretation of the state inheritance tax law; if the state tax was imposed on the right to transmit, the deduction could only be claimed by the estate, if the state tax was imposed upon the right to inherit, the deduction could only be claimed by the beneficiary. One of the purposes of Sec. 703 was to save deductions where the payment or the claim to the deduction had been made by the wrong party, and the period for the right party to claim the deduction had expired. The wrong party was the party—whether the beneficiary or the estate—upon whom the state statute did not impose the tax.

Thus in the report of the House Committee on Ways and Means, in regard to this section, it was said:

> "* * * As a result of recent Supreme Court decisions (Keith v. Johnson and United States v. Mitchell), redeterminations of the deductions claimed by the estate or by the beneficiary will be necessary unless the situation is remedied by retroactive legislation. Consequently your committee deems it advisable to insert section 705 in the bill, the general effect of which will be to ratify what the taxpayers have done and to prescribe specific rules for future action." (Quoted on Page 42 of original brief and published in Cong. Doct. 8831).

Section 703 contemplates that the determination may be made after the right of the beneficiary or the

right of the estate is barred by limitations and hence subparagraph (5) was inserted to cover this very situation.

III.

THE DISTRICT COURT ERRED IN HOLDING THAT THE FACT THAT THE AMOUNT OF THE CALIFORNIA INHERITANCE TAX WAS ALLOWED AS A CREDIT AGAINST THE FEDERAL ESTATE TAX WOULD PREVENT THE PETITIONER FROM CLAIMING A DEDUCTION FOR HER SHARE OF THE CALIFORNIA INHERITANCE TAX IN HER PERSONAL INCOME TAX RETURN.

The opinion of the Court of Appeals did not discuss this question, and the effect is to leave unchallenged the ruling of the District Court on this question of the interpretation of the Revenue Act.

In the Third Conclusion of Law, the District Judge rules:

> "The estate having had the benefit of a credit for the entire $294,752.61 inheritance tax in the Federal estate tax return as the result of representations to the Commissioner, by plaintiff and her co-executors, that the executors had paid the same, plaintiff in equity and good conscience may not now be heard to assert that she paid $92,451.56 thereof in her individual capacity."

In answer to this conclusion, we respectfully submit:

(a)—The record contains no evidence that any representation was made by the petitioner or her co-executors to the Commissioner, that the executors had paid the California inheritance tax of $294,752.61.

(b)—The estate was entitled to a credit for the amount of the California inheritance tax as against

the amount of the Federal estate tax, whether the California inheritance tax was paid by the estate or was paid by the beneficiaries.

The representation, even if made, would be wholly immaterial.

In other words, the law gave two separate and independent rights:

(1)—The right to the estate to credit against the Federal Estate Tax, 25% of the amount of any estate, inheritance, legacy or succession taxes paid to a state by the estate or by the beneficiaries.

(2)—The right to the beneficiary, under Section 703, to deduct his share of such inheritance tax from his gross income in the year in which that tax was paid.

The first is the right to a credit against tax and the second is the right of deduction from gross income.

Section 301 (b) of the Revenue Act of 1924, Title III, Part I, provides:

> "The tax imposed by this section shall be credited with the amount of any estate, inheritance, legacy or succession taxes actually paid to any State or Territory or the District of Columbia, in respect of any property included in the gross estate. The credit allowed by this subdivision shall not exceed 25 per centum of the tax imposed by this section."

It will be noted that the language used is "taxes actually paid to any state * * * in respect of any property included in the gross estate".

The only requirement is that the state tax shall have been paid in respect of property included in the gross estate.

The statute does not say by whom it needs to be paid.

An inheritance tax is upon the right of a beneficiary to inherit. A legacy tax is upon the legatee. A succession tax is upon the right of the beneficiary to succeed.

The retroactive Section 703 of the Revenue Act of 1928 specifically regulated the right to deduct state inheritance taxes in the income tax returns of the estate and of the beneficiary. Subject to the conditions in Section 703, the right might be claimed by the estate or by the beneficiary.

The right to a credit against the Federal Estate Tax for state inheritance taxes paid by a beneficiary was expressly recognized by the Estate Tax Regulations. Article 9 (a) of Regulations 70 (1926 edition) provided that—

> "Before the Commissioner allows any credit for any estate, inheritance, legacy, or succession taxes, there must be submitted to him the following: (3) An affidavit of the executor stating whether any litigation has been instituted, or appeal taken, or any such action is designed or contemplated by him, or, to his knowledge, *by any beneficiary* or other person, the final determination of which may affect the amount of such taxes."

A similar provision was made in Article 9 (a) of Regulations 68 (1924 edition).

Respectfully submitted,

H. F. STAMBAUGH,
Attorney for Petitioner.